BACKGROUND INFORMATION PREPARED BY THE

DEPARTMENT OF AGRICULTURE

BLENDED CREDIT FOR COTTON TO KOREA

March 4, 1983

United States Department of Agriculture

Foreign Agricultural Service

Washington, D.C. 20250

MAR 4 1983

TO: Alan T. Tracy
Acting Under Secretary for
International Affairs and Commodity Programs

FROM: Richard A. Smith
Administrator

Dick S

SUBJECT: Background Information Regarding Blended Credit for Cotton to Korea

Attached is the background paper you requested outlining the pros and cons of extending blended credit to the Koreans for purchases of U.S. cotton. We are also attaching a copy of the February 15 memorandum to the Secretary regarding this issue and a copy of the cabinet decision paper which went to the Secretary during your absence last week.

The direct costs to the U.S. Government for the $10 million interest free credit for 30 months would be $1.7-1.9 million but the direct benefits would be $26-29 million in savings under the most likely scenario outlined in the attached paper. Far more important over time would be the positive effect of blended credit and credit guarantees in maintaining our traditional share (90-95 percent) of the Korean cotton market. Without this small investment by the United States, U.S. cotton industry analysts and we are convinced that our share of the Korean market will trend downward over time toward the market shares we had in 1981/82 in Japan (45.0 percent), Taiwan (61.8 percent) and Hong Kong (33.6 percent).

Cotton's share of the additional $1.25 billion blended credit authorization is in line with cotton's share of U.S. agricultural exports (see attached table), and we believe the benefits in terms of increased exports and domestic program savings would be equal to those for other major agricultural exports.

Attachments

What would be the savings to the US Government of a $50 million blended credit cotton program for Korea?

The cost to the U.S. Government of the blended credit proposal would be the loss of interest for 30 months on the $10 million direct credit portion of the loan. This would total about $1.7 to 1.9 million.

The potential cotton program cost to the U.S. Government could be much higher if blended credit is not authorized. The 86,000 bales of cotton that would be exported under the proposal, if redeemed from loan stocks, would save CCC $26 to 29 million- the cost of releasing 86,000 bales to producers under the PIK program. At the present time about 7.1 million bales are under loan. The current 1983/84 U.S. production forecast is 9.5 million bales.

The potential longer term cotton program costs of not providing the blended credit now could be much higher should the U.S. share of the Korean market decline sharply from the 90-95 percent traditional level.

How much of the Korean cotton market will we lose if we do not provide blended credit?

The latest industry estimates project a market loss of 1.2 million bales over the next 3 years (1983-84-85) valued at $452 million. Their projections show our market share slipping from about 90 percent to about 60 percent.

The U.S. share of the Korean cotton market is unusually high reflecting the effectiveness of our credit programs and close political and economic ties. Our market share in 1981/82 in Japan was 45 percent, in Taiwan 61.8 percent and in Hong Kong 33.6 percent.

Who are the countries that are currently competing with the U.S. for the Korean cotton market?

At the moment, Australia, Brazil, India, Pakistan and the Sudan are all trying to gain a larger share of the Korean market at the expense of the United States cotton producers. The trade safeguard provisions that will be incorporated into all blended credit programs will protect the traditional market share of nonsubsidizing countries.

Are the Koreans threatening to reduce cotton imports from the U.S. to obtain blended credit?

The U.S. has already begun to lose market share in Korea as a result of aggressive action taken by other cotton suppliers to break into the large Korean market. Also, there are strong internal and external pressures to diversify cotton imports to help address Korea's trade surplus with several other cotton suppliers.

Korean Cotton Imports

Period	Country	Percent Market Share
Jan/July 1982	U.S.	95.1
	All Others	4.9
Aug/Nov 1982	U.S.	88.6
	All Others	11.4
Dec 1982/	U.S.	79.8
Feb. 11, 1983	All Others	20.2

The Korean Spinners and Weavers Association now control all cotton imports and favors trade with the U.S. due in large part to our credit arrangements, strong trade ties and reliability as a supplier. Without the credit programs, ties to the U.S. would be weaker and it is possible that control of cotton imports would shift to a Korean Government Agency or to private trading companies. This shift would likely have a negative impact on our share of Korean imports.

Does the Korean textile industry need blended credit and credit guarantees?

The Korean textile industry has suffered from the world recession and a number of firms are facing severe financial problems. Their financial situation, however, is not our primary concern. Our concern is how these programs help expand markets for U.S. cotton and reduce our farm program costs.

What effect will the blended credit have on U.S. textile imports from Korea?

Imports of cotton textiles into the United States from Korea are limited by the United States-Korea bilateral agreement negotiated under the Multi-Fiber Arrangement. Blended credit for Korea would have no bearing on the level of U.S. cotton textile imports. Korea can be expected to continue to fill its U.S. import quotas, whether the textiles are made from U.S. or foreign cotton.

Are we providing aid to the Koreans through our credit programs?

Without question past PL 480 sales greatly assisted in the economic development of Korea. Current credit guarantees and the proposed blended credit program would provide important but limited benefits to the Korean textile industry, but the primary beneficiaries would be the U.S. cotton producer and the U.S. Treasury (see cost discussion above).

Will the cotton industry continue to press for their fair share of available credit?

The U.S. cotton industry has been interested since the 1940's in securing credits as an aid to their efforts to expand our foreign markets for U.S. cotton. It is certain their requests for credit assistance will continue for the forseeable future as they have had a number of success stories. The outstanding success story is Korea. This market has progressed from one quarter of a million bales at the end of the Korean war to a one and half million bale market today, primarily due to the extensive use of concessional PL 480 financing during the fifties and sixties and short term commercial credits and guarantees during the seventies and the eighties.

What is cotton's share of the blended credit program?

An analysis of the potential recipients of the additional $1.250 billion available under the blended credit program for fiscal year 1983 as reflected in the potential list of $1,890 billion clearly shows that the raw cotton share of 5.5 percent is in parallel with cottons percentage share of total agricultural exports (see attached table).

U.S. Agricultural Exports (Billion $)

Potential Additional Blended Credit Program (BC) (Million $)

Commodity	FY 1982	Percent	Forecast FY 1983	Percent	BC	Percent
Raw cotton..	2.141	5.5	1.6	4.4	105	5.5
Wheat & Prod	7.675	19.6	6.8	18.9	846	44.7
Feed Grains.	7.051	18.1	6.7	18.6	345	18.3
Rice........	1.149	2.9	0.9	2.5	264	14.0
Oilseeds & Prod.......	9.730	24.9	9.1	25.3	191.1	10.1
Others......	11.348	29.0	10.9	30.3	139.25	7.4
Total......	39.094	100	36.0	100	1890.35	100

Tobacco, Cotton and Seeds Division
March 3, 1983

DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D. C. 20250

CABINET MATTER ________

I SUBJECT: Approval of Blended Credit to enable export of cotton to Korea

II ORIGINATOR: Department of Agriculture

III ACTION FORCING EVENT: Need to increase exports of cotton to limit Commodity Credit Corporation (CCC) program outlay and to meet foreign competition.

IV STATEMENT OF THE ISSUE: The Department of Agriculture in the face of rising cotton program outlays seeks cabinet approval to authorize a 36 month blended credit program consisting of $10 million GSM-5 and $40 million GSM-102 that would enable export of cotton to Korea.

V ANALYSIS: The domestic price of U.S. cotton is hovering at the loan level because of large stocks and reduced export prospects due to world recession and keener foreign competition. Commodity Credit Corporation outlays for the cotton program will be more than $1.5 billion in FY 1983. Use of blended credit to assist exports would reduce stocks and help restrict potential CCC loan outlay. A blended credit program for Korea would help the United States maintain its share of a market that has been developed through long-term promotion effort.

A blended credit program consisting of $10 million in GSM-5 direct credit and $40 million in GSM-102 guarantees will finance export of 143,000 bales ($50 million) of cotton to Korea in 1983; 86,000 bales of this would not be exported without blended credit. Reduction of domestic stocks by 86,000 bales will remove cotton which could go under loan at a cost of $24.5 million in CCC direct outlay.

Korea is now the second largest foreign market for U.S. cotton accounting for nearly 30 percent of total U.S. exports. The United States dominant supplier position (consistently more than 90 percent of Korea's cotton imports) is the result of more than a decade of diligent promotion effort by the U.S. cotton industry in cooperation with USDA. The United States share of the Korean market is being eroded by cheaper foreign growths.

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Several competitors are now offering cotton to the Koreans at prices below our prices for comparable quality. The lower price quotations by some competitors (e.g. Brazil) reflect, in part, production and export aids designed to break into the large Korean cotton market.

Spinners and Weavers Association of Korea (SWAK) member mills would prefer to continue to rely on U.S. cotton for the great majority of their needs. However, they are experiencing a cost-price squeeze due to the slump in textile demand, the impact of high interest rates on financing of raw cotton purchases and the strength of the dollar. They are being forced to turn to cheaper sources of supply. It could be very difficult for U.S. exporters to regain their traditional share of Korea's market, once it is lost.

Blended credit would reduce the cost of purchasing U.S. cotton and demonstrate to SWAK that the United States intends to remain a dependable supplier.

VI

RECOMMENDATION: USDA be given authority to extend blended credit for cotton to Korea.

VII DECISION:

____Approve _______Approve as amended _____Reject ___ No Action